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July 27, 2005

Mr. Jonathan G. Katz
Secretary
U.S. Securities and Exchange Commission
100 F Street, N.W.
Washington, D.C. 20549-9303

Re: Petition for Rulemaking Under Rule 192 of the SEC's Rules of Practice Concerning Extended Implementation Date in Rule 202(a)(11)–1(b)(2) Under the Investment Advisers Act of 1940

Dear Mr.Katz:

The American Council of Life Insurers (ACLI) respectfully requests a reasonable extension of the October 24, 2005 date for compliance with section (b)(2) in new Rule 202(a)(11)–1 under the Investment Advisers Act of 1940. ACLI has 299 members representing 83% of the life insurance business. Many of our members manufacture variable life insurance and variable annuities that are distributed through registered broker-dealers.

New Rule 202(a)(11)–1 under the Investment Advisers Act of 1940 clarifies the scope of the broker-dealer exclusion from the definition of investment adviser. The new rule has an important impact on broker-dealers affiliated with life insurers that will require significant systems and structural changes. A reasonable extension to the compliance date for Rule 202(a)(11)–1(b)(2) would help reduce burdens confronting the life insurance industry under the new rule.

Regulatory Background and Issue Presented

The principal impact of the new rule on life insurers involves the broker-dealer exclusion from the definition of investment adviser. Section 202(a)(11) defines investment advisers as persons who receive compensation for providing advice about securities as part of a regular business. Section 202(a)(11)(C) provides an exclusion from the definition of investment adviser for brokers or dealers " whose performance of investment [advisory] services is solely incidental to the conduct of his business as a broker or dealer and who receives no special compensation therefore." The SEC has issued several releases over the years interpreting this definitional exclusion in light of evolving securities, advisory and financial planning practices.[1] In the same way, new Rule 202(a)(11)–1 provides updated guidance on the scope of the broker-dealer exclusion from the definition of investment adviser, among other things.

[1] *See* Investment Advisers Act Rel. No. 1092 (Oct. 8, 1987)[52 FR 38400 (Oct. 16, 1987)]

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Under Rule 202(a)(11)–1(b)(2), a broker-dealer would not be providing advice *solely incidental* to brokerage if it provides advice as part of a financial plan or in connection with providing planning services and: (i) holds itself out generally to the public as a financial planner or as providing financial planning services; or (ii) delivers to its customer a financial plan; or (iii) represents to the customer that the advice is provided as part of a financial plan or financial planning services.

According to the adopting release, a broker-dealer that provides investment advice and delivers a financial plan to a customer or represents to a customer that its advice is provided as part of a financial plan or in connection with financial planning services must register under the Advisers Act and treat that customer as an advisory client. The deadline for compliance with Rule 202(a)(11)–1(b)(2) is October 24, 2005.[2]

The release explains that financial planning services typically involve assisting clients in identifying long-term economic goals, analyzing their current financial situation, and preparing a comprehensive financial program to achieve those goals. The release also notes that a financial plan generally seeks to address a wide spectrum of a client's long-term financial needs, including insurance, savings, tax and estate planning, and investments, taking into consideration the client's goals and situation, including anticipated retirement or other employee benefits. Many of these functions have historically been performed in traditional life insurance distribution as ingredients of fact finding and needs-based recommendations.

Several aspects of Rule 202(a)(11)–1(b)(2) may have an impact on life insurance agents who are registered representatives of a broker-dealer. Because broker-dealers affiliated with life insurers are significantly different from full-service broker-dealers, compliance with Rule 202(a)(11)–1(b)(2) will present different compliance and timing challenges, which are highlighted below.

The Unique Nature of Broker-Dealers Affiliated with Life Insurers

Many broker-dealers affiliated with life insurance companies are significantly different from full service or "wire-house" broker-dealers in their structure, operations, products and services.[3] The securities activities of broker-dealers affiliated with life insurers are a component of a larger insurance business. Many registered representatives operate principally as life insurance and

[2] *See* Investment Advisers Act Rel. No. 2376 (Apr.12, 2005)[74 FR 20424 (Apr. 19, 2005) at 20442]

[3] Several examples help demonstrate the different characteristics of broker-dealers affiliated with life insurers. The range of products offered by these limited purpose broker-dealers is typically narrow and focuses upon the distribution of variable insurance contracts and mutual funds. It may be helpful to consider those securities activities and services *not* offered by most broker-dealers affiliated with life insurers. Typically, these firms do not maintain discretionary accounts permitting registered representatives to purchase and sell securities on behalf of a client without specific approval of each transaction. On an industry-wide basis, these broker-dealers generally do not take custody of client funds, securities or assets. This type of firm does not typically "carry" customer accounts. Insurance broker-dealers usually require that payment for variable insurance or securities products be made by check payable to the processing office, and not by check payable to the agent/registered representative. Variable contracts and shares in investment companies are issued directly to purchasers and do not constitute bearer instruments. Broker-dealers affiliated with life insurers generally do not maintain "open accounts" or facilitate the implementation of stop orders and limit orders, which obviates many potential brokerage problems. Broker-dealers affiliated with life insurers do not make markets in securities or underwrite new issues of securities. In several instances, the federal securities laws and the NASD regulations provide appropriate regulatory exceptions because these limited purpose broker-dealers are different from full service broker-dealers.

annuity salespersons. In some business models, securities sales and investment advisory activity are small relative to traditional insurance product sales by an office or registered representative.

Broker-dealers affiliated with life insurers often conduct supervision and compliance through an insurance distribution system. Consequently, registered representatives of broker-dealers affiliated with life insurers often conduct business in small, geographically dispersed offices. Many registered representatives affiliated with life insurers currently operate appropriately in non-branch locations.[4] In contrast, full-service firms generally tend to have many more sales people report to a number of large branch offices. Full service firms' existing compliance infrastructures may be adapted to include the delivery of advisory services. The rule's compliance date, therefore, is more logistically complex for insurance affiliated broker-dealers than for full-service firms.

An example may help vivify the burden of the October 24, 2005 compliance deadline on the life insurance industry. One of our member life insurers has approximately 7,000 life insurance agents who are registered representatives of an affiliated broker-dealer. These life insurance agents typically have a Series 6 NASD license authorizing the sale of variable life insurance, variable annuities, and mutual funds, and derive the bulk of their income from insurance sales. As a technological extension of the life insurer's emphasis on fact-finding and needs-based recommendations, the company provides qualified agents access to proprietary planning software that generates custom tailored reports based on information customers provide about their financial background and objectives.

The company's planning software can address a variety of topics, including: survivor income; disability protection; long term care planning; retirement planning; education planning; estate planning; major purchase funding; and, asset allocation. Several of these topics focus on traditional insurance planning issues supported by fact-finding and customer needs. This insurance company has historically made the reports available to customers without charge or obligation. The life insurer spent millions of dollars developing the software and training its agents to use the program for appropriate recommendations and sales. The NASD has reviewed and approved the program for use by registered representatives.

Following the adoption of Rule 202(a)(11)–1(b)(2), the use of a planning program in this fashion may preclude continued reliance on the broker-dealer exclusion from the definition of investment

[4] NASD Conduct Rule 3110 defines the term "branch office" as any business location of the broker-dealer identified to the public or customers by any means as a location at which the investment banking or securities business is conducted on behalf of the member. *See* NASD Conduct Rule 3110(g)(2) (2004).The NASD definition excludes any location identified solely in a telephone directory line listing or on a business card or letterhead, which listing, card, or letterhead also sets forth the address and telephone number of the office of the broker-dealer responsible for supervising the activities of the identified location. The NASD has issued two interpretations embellishing this position. *See* 4 NASD Regulatory and Compliance Alert 1 (Feb. 1990) at 7 (clarifying interpretations on branch office communications) and NASD Notice to Members 89-34 (Apr. 1989) at 204 (clarifying the meaning of business advertisements and public listings). The scope of the branch office definition has significant compliance and regulatory implications for broker-dealers. Compliance procedures must be tailored to the nature and volume of business of each location. It should be noted in the interest of full discussion that the NASD has proposed an amendment to the definition of the term "branch office" that has been filed with the SEC for approval. See Rel. No. 34-51742; (May 25, 2005) which can be found at http://www.sec.gov/rules/sro/nasd/34-51559.pdf . The amendment would revise the threshold for branch and non-branch locations of a broker-dealer. ACLI has filed a letter of comment on this proposal which can be found at http://www.sec.gov/rules/sro/nasd/nasd2005030/acli062305.pdf .

adviser because the planning program is no longer construed to be "solely incidental" to the broker-dealer business. As a consequence, many of the life insurer's 7,000 NASD registered agents may need to become investment advisory representatives. The magnitude of this regulatory status transformation and the unique characteristics of broker-dealers affiliated with life insurers make the rule's October 24, 2005 compliance deadline very challenging and perhaps unachievable. The scope and factors highlighted above will be faced by a number of our member life insurers. This is not an isolated example.

The logistics of such a large scale transformation are daunting. Although the life insurer has a small investment advisory affiliate, the infrastructure to support such a large scale increase will consume time and resources in planning and execution. The short-term transformation would also strain the life insurer's broker-dealer supervisory services, which were not designed to quickly integrate Advisers Act compliance procedures. Such a large scale transformation also requires coordination of many small, non-branch locations that are geographically dispersed. In contrast, full-service broker dealers typically have most registered representatives operating out of larger branch offices that may be easier to integrate into the new rule's requirements.

Our members understand the importance of the new rule and the need to fulfill its standards. Many companies have made significant headway in identifying agents whose activities now trigger registration as investment advisory representatives. Our members are endeavoring to make good faith compliance with the new rule as promptly as possible. It is our belief and concern that even with best efforts and good faith, some companies will be unable to fulfill the enterprise-wide transformation for all investment advisory representatives by the October deadline due to the unique features of broker-dealers affiliated with life insurers, and the scope of the transformations required.[5]

Relief Requested

The deadline for compliance with Rule 202(a)(11)–1(b)(2) will have a unique, disproportionate impact on broker-dealers affiliated with life insurers because of the differences in their structure and operations compared to full-service broker-dealers. These differences could unnecessarily burden broker-dealers affiliated with life insurers, and warrant a reasonable extension of the October 24, 2005 compliance deadline.

Former SEC Chairman Levitt emphasized the importance of reviewing the impact of rulemaking on efficiency and competition when he stated:

> In response to the National Securities Markets Improvement Act of 1996 (NSMIA), the Commission has rededicated itself to considering how rules affect competition, efficiency, and capital formation as part of its public interest determination. Accordingly, the Commission intends to focus increased attention on these issues when it considers rulemaking initiatives. In addition, the Commission measures the benefits

[5] The release adopting the rule notes that transformation of registered representatives to investment advisory representatives will require broker-dealers to create new disclosures, redraft contractual language, and create processes for developing, delivering, and managing these new materials.

of proposed rules against possible anti-competitive effects, as required by the Exchange Act.[6]

There are several policy considerations supporting our request for a reasonable extension to the rule's October 24 compliance deadline. Although the SEC exercised commendable rulemaking diligence in proposing the rule twice, the implementation deadline of Rule 202(a)(11)–1(b)(2) was not a subject of the two proposals. The staff's ultimate determination on the narrowed scope of the "solely incidental" caveat to the broker-dealer exclusion from the investment adviser definition was not crystallized clearly until the adopting release. Neither the SEC nor the life insurance industry, therefore, could have fully appreciated the impact of the interpretive change on broker-dealers affiliated with life insurers. Since the rule was not primarily focused on these types of broker-dealers, it is understandable that the impact of the deadline on them was not a matter of specific focus. Nothing in the adoption release identified a critical reason for the specific October 24 deadline. A reasonable compliance extension, therefore, is warranted under these circumstances.

A reasonable extension would not greatly impair consumers. With an extension, registered representatives of broker-dealers affiliated with life insurers can be integrated into the new rule's requirements in an orderly fashion that responsive to the unique characteristics of this segment of the broker-dealer world. In contrast to many other registered representatives, life insurance agents must also fulfill state insurance laws and regulations, which provide additional meaningful consumer protection, such as free-look provisions, replacement regulation standards, buyers' guides, disclosure regulations, and proscriptions under Unfair Trade Practices Acts, among many others.

The traditional fact-finding and need-based approaches to insurance sales fulfill consumer interests by matching consumer needs with product recommendations. This approach helps consumers make informed purchase decisions, and has been a constant component of insurance distribution well before the advent of financial planning. Adherence to the October deadline may interrupt the delivery of needs-based planning tools, which may conflict with the best interests of consumers who can benefit from comprehensive approaches to decision making.

For the reasons discussed above, we respectfully request that the compliance deadline be extended for six months until April 24, 2005. This brief extension should allow broker-dealers affiliated with life insurers to fulfill the requirements of the new rule for salespersons or offices that will trigger the definition of investment adviser under Rule 202(a)(11)-1. In other rulemaking, the SEC has granted reasonable extensions to compliance dates for good cause. A brief extension relieves unnecessary burdens, and reflects the purposes of the Advisers Act.

A reasonable six month extension would balance regulatory goals against unanticipated rulemaking burdens. An implementation delay would sensibly integrate different segments of the

[6] *See* testimony of Arthur Levitt, SEC Chairman, concerning appropriations for fiscal year 1998 before the Subcommittee on Commerce, Justice, and State, the Judiciary, and Related Agencies of the House Committee on Appropriations (Mar 14, 1997), which appears at http://www.sec.gov/news/testimony/testarchive/1997/tsty0497.txt

financial services industry into the new rule.[7] A compliance deadline with a reasonable and deliberative roll out for insurance agents who are registered representatives makes good rulemaking sense.

I greatly appreciate your attention to our views. Please let me know if any questions develop or if we can provide any additional information that would be helpful.

Sincerely,

Carl B. Wilkerson

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Cc: The Honorable Cynthia A. Glassman, Acting Chairman
The Honorable Paul S. Atkins, Commissioner
The Honorable Roel C. Campos, Commissioner
The Honorable Harvey J. Goldschmid, Commissioner
Giovanni Prezioso, General Counsel
Robert E. Plaze, Associate Director, Division of Investment Management
Nancy M. Morris, Attorney-Fellow
Robert L. Tuleya, Senior Counsel

[7] An extended compliance deadline also allows entities in need of interpretive clarification under the rule to reasonably integrate the impact of specific clarifications.